

## Chapter 9 – Leases

### Introduction

This chapter covers the following areas on leases:

- A. Service Negotiated Leases
- B. Capital Leases
- C. Leasehold Improvements


### A. Service Negotiated Leases

#### POLICY

##### Service negotiated leases

Space and real property leasing requirements for the Regional Division of Contracting and General Services (CGS) office include:

1. If the Service is going to acquire space or land by lease, the General Services Administration (GSA) must be contacted first. GSA must certify that no suitable space meeting the Service requirements is available in GSA's portfolio.
2. A delegation of authority must be requested if the Regional office (RO) desires to acquire the space (real property) unless the requirement meets the categorical exclusions found in *CFR 102-73.150*. GSA will delegate leasing authority when it is economically feasible, expediency is required, or it is in the best interest of the Government.
3. All space requests must be forwarded to the chief, Division of Contracting and Facilities Management (CFM) Washington office, with the exception of lease renewals in which there is no change in the space assigned.
4. The program offices, in conjunction with the Regional CGS, will determine the appropriate delineated area for space and facilities and certify that the location decision is in compliance with *Title 41, Section 102-79.55 - 90*.
5. All lease actions must be accomplished in accordance with the appropriate provisions of the Federal Acquisition Regulation and any supplemental guidance which GSA may issue.

 **Before a lease action can begin:** When a determination had been made to acquire space by lease, the Service must first try to find a suitable, available space in government-owned and government-leased buildings. If a suitable government-controlled space is unavailable, a lease may be executed.

**GUIDANCE**

Who can  
acquire leased  
space or real  
property?

An employee of a program office may not directly or indirectly contact potential lessors for the purpose of acquiring space on behalf of the Service. GSA acquires leased space and real property for all Federal agencies under its specific statutory authority. The sole point of contact with GSA on all space related matters will be the Regional office division of CGS Washington office CFM.

Only warranted lease contracting officers may acquire leases on behalf of the Service. If the Service is going to acquire space or land by lease, GSA must be contacted first to determine whether space is available in GSA's portfolio. A delegation of authority from GSA must be requested if RO desires to acquire the space/real property. GSA will delegate leasing authority when it is economically feasible, expediency is required, or it is in the best interest of the Government.

**PROCESS**

What to do for a  
lease acquisition

The program offices will prepare the following and submit to the Regional CGS office:

- *Request for Space and a Space Requirements Worksheet*, using a format acceptable to the Region.
- A memorandum to the Assistant Director – Business Management and Operations (ABMO), justifying the need for the space. The memo should include the organization and subactivity code originating the request so the cost for the space may be properly distributed.
- Annual estimated cost for the space

**POLICY**


Rural  
Development  
Act  
Requirement

The Rural Development Act of 1972 (RDA) requires that the first priority be given to locating new facilities in rural areas. The Farm Security and Rural Investment Act of 2002, PL 107-71 defines rural and rural area as any area other than a city or a town that has a population of more than 50,000 inhabitants, and/or the urbanized area contiguous and adjacent to such a city.

**POLICY**

Requirements  
for long and  
short term lease  
durations

Requirements for long term and short term lease durations include:

<b>Long term lease</b>	Leases executed by the Service may be for a term, including all options, of up to 20 years. However, land if unimproved, may be leased only on a fiscal year basis.
<b>Short term lease</b>	<p>If there is a need for short term use, such as conferences and meetings, judicial proceedings, and emergency situations, RO must first contact GSA and inquire whether there is Government-controlled space which may be available.</p> <p>If no suitable government controlled facility is available, the CGS office may lease a commercial facility for a term not to exceed 180 days.</p> <p> GSA must approve extensions beyond 180 days.</p>

**GUIDANCE**

Rules for acquiring leasehold interests for build to suit leases

When acquiring leasehold interests in buildings to be constructed for Service use, the lease contracting officer must:

- Assure that detailed building specifications have been developed before agreeing to a lease that will result in the construction of a building.
- Use competitive procedures. The requirements in the *Competition in Contracting Act* must be followed.
- Conduct inspections during and after construction of assure that the building complies with previously detailed specifications.
- Ensure that the lease contains provision permitting the Service to reduce rent during any period when the building does not comply with the Service's specifications.

☞ When the Service has the authority to execute its own leases, the CGS warranted contracting officer may negotiate with an offeror to ensure any proposed lease scores as an operating lease.

**GUIDANCE**

When to consider acquiring leases with purchase options

The Service may consider leasing with a purchase option at or below fair market value, when one or more of the following conditions exist:

- The purchase option offers economic and other advantages to the Service and is consistent with the Service's goals.
- The Service will be the sole or major tenant of the building and has a long term need for the property.
- Leasing with a purchase option is in the best interest of the Service.

☞ It should be noted that leases with purchase options are typically capital leases. It is important to complete the *Capital and Operating Determination Worksheet* and any subsequent budget scoring which may be required.

**PROCEDURE**


How to report requirements for serviced leased space

The Service is required to report Service leased space on the annual basis. Use the steps below to report requirements for Service leased space:

Step	Action
1	Report Service leased space on the annual <i>Space Budget and Justification, Exhibit 54</i> , which is used by OMB to prepare the President's Budget.
☞	Complete. Ready for filing.

The Regional CGS offices will submit the following information to the CFM Washington office:

Step	Action
1	A copy of each lease with all appropriate documentation including a copy of the delegation of leasing authority and the completed <i>Capital and Operating Lease Determination Worksheet</i> , immediately after the lease award.
2	A list of Service leased space in a spreadsheet format includes: <ul style="list-style-type: none"> <li>• Location of the space</li> <li>• Lease term</li> <li>• Annual cost</li> <li>• Cost per square foot</li> </ul>

	<ul style="list-style-type: none"><li>• Occupancy date</li><li>• Number of parking spaces</li></ul>
	Complete. Ready for filing.

## B. Capital Leases

### Introduction Capital leases

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A capital lease is a lease that transfers substantially all the benefits and risks of ownership to the Service. These leases are capitalized as a Service asset.


The determination of whether a lease will be a capital lease is accomplished well in advance of the acquisition because of the possible budget scoring that may be required.

### POLICY Capital leases

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A lease is considered to be a capital lease when one of the four criteria below is met.

1. Ownership of the property is transferred to the Service at or shortly after the end of the lease term.
2. The property may be purchased at a bargain price at the end of the lease term.
3. The lease term is greater than 75% of the estimated economic useful life of the asset.
4. The present value of the minimum lease payments over the life of the lease is greater than 90% of the fair market value of the asset at the beginning of the lease term.

 The Service should avoid capital leases. With a capital lease, there is a possibility that rental payments over the life of the lease may exceed the value of the property. Therefore, it may be more economically feasible to construct a building rather than lease a building or execute a lease-purchase agreement.

**PROCESS**

Capitalized and  
operating lease  
decision process

Use the following process to make a capitalized and operating lease decision:

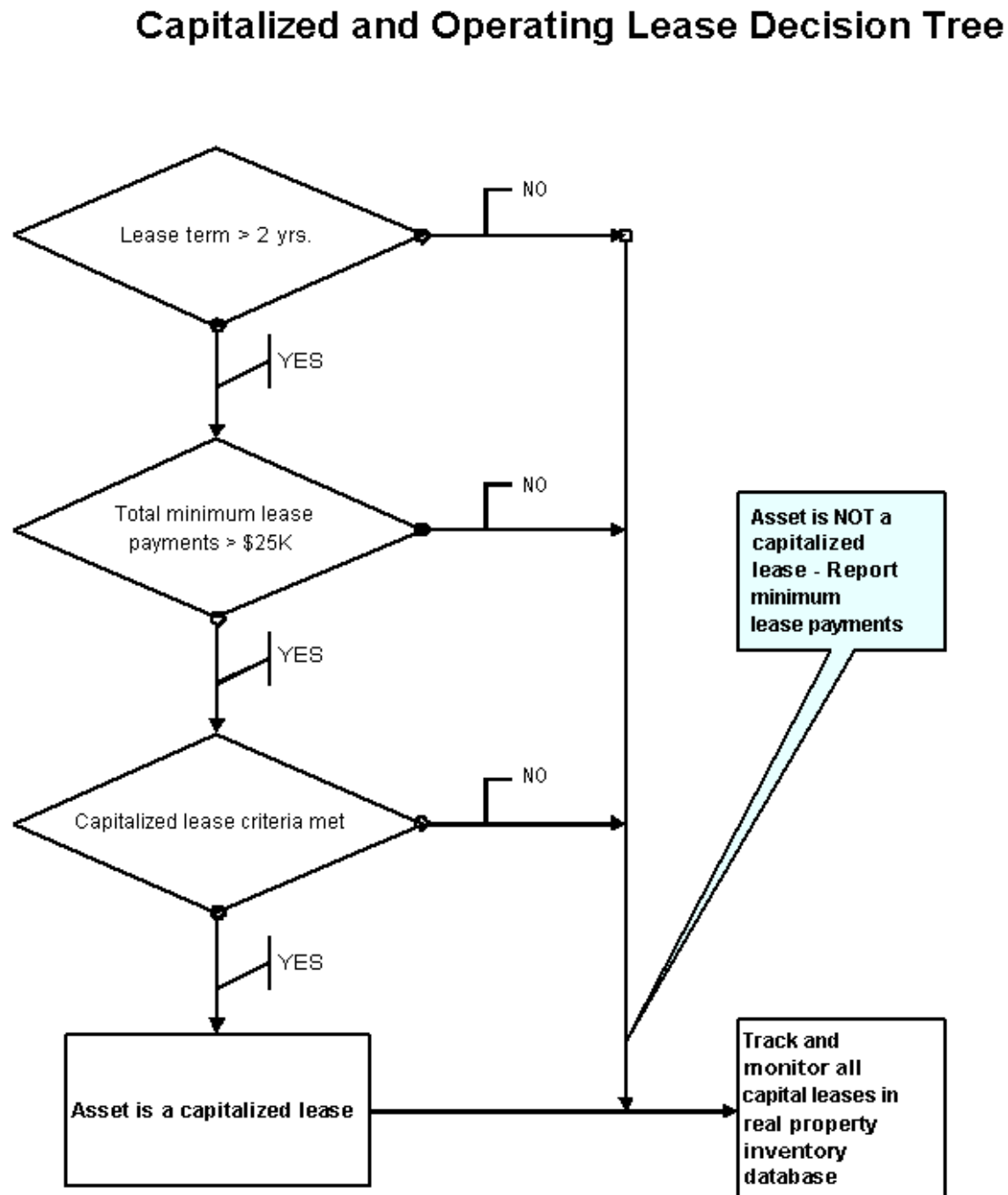


Figure 3 - Capitalized and Operating Lease Decision Tree

**GUIDANCE**

How to  
determine  
capital versus  
operating  
leases

The following spreadsheet applies the criteria in SFFAS 5 to determine if a lease should be classified as a capital lease. If it results in a determination of capitalization, the BFO will notify FC of the lease cost, acquisition date, and identify FFS source documents.

☞ A copy of Determination of Capital versus Operating Leases must be kept in each official lease file.

**Part A - Input the following information:**

Description of lease/asset:		
Date of lease:		
Information from the lease:		
Noncancelable lease term (years)	- 0	If the likelihood that the government will cancel the lease before expiration is remote, then terms related to the <i>availability of funds</i> should not be considered in determining the noncancelable lease term.
Annual lease payment (\$)		
Cost to purchase asset at end of lease		If the lease does not contain a purchase arrangement, enter "N/A." Otherwise, enter a \$ amount.
Information about the asset: Estimated total useful life of the asset (years)	1.0	
Age of asset at lease inception (years)	- 0	If new, enter 0
Value of leased asset at lease inception: (\$) What is the asset worth today?		
Estimated value of asset at end of lease: When the noncancelable term is up.		
Other information: Interest rate	0.00%	Use <i>Daily Treasury Yield Curve Rate</i> for time period closest to lease term. See <a href="http://www.treas.gov/offices/domestic-finance/debt-management/interest-rate/index.html">www.treas.gov/offices/domestic-finance/debt-management/interest-rate/index.html</a>

**Part B - Circle "Yes" or "No" in response to each question:**

☞ One or more "Yes" answers indicate a capital lease.

Yes/No	<b>Step 1.</b> Does the lease transfer ownership of the property to the lessee by the end of the noncancelable lease term?									
Yes/No	<b>Step 2.</b> Does the lease contain an option to purchase the leased property at a bargain price?	<div>Cost to purchase asset at the end of lease</div> <div><ul style="list-style-type: none"><li>Estimated asset value at the end of lease</li><li>Would a reasonable person consider the purchase price to be a bargain that would almost ensure that the option to purchase is exercised? If “Yes”, the lease is a capital lease.</li></ul></div>								
<b>Step 3 and 4</b> Do not apply if asset is in the last 25% of its useful life:		<table><tr><td>Total useful life of asset</td><td>1.0</td></tr><tr><td>Current age of asset</td><td><u>- 0</u></td></tr><tr><td>Remaining useful life</td><td>1.0</td></tr><tr><td>Percent of useful life remaining</td><td>100.0%</td></tr></table>	Total useful life of asset	1.0	Current age of asset	<u>- 0</u>	Remaining useful life	1.0	Percent of useful life remaining	100.0%
Total useful life of asset	1.0									
Current age of asset	<u>- 0</u>									
Remaining useful life	1.0									
Percent of useful life remaining	100.0%									

Yes/No	<b>Step 3.</b> Is the lease term greater than or equal to 75% of the estimated economic life of the leased property?	Estimated useful life (yrs)	1.0
		X 75%	75%
		= 75% of estimated economic life	0.8
		Noncancelable lease term (yrs)	<u>  0  </u>
		Difference	0.8
		If the difference is negative the lease is a capital lease.	Answer "No"
Yes/No	<b>Step 4.</b> Does the present value of rental and other minimum lease payments, excluding that portion of the payments representing executory cost, equal or exceed 90% of the fair value of the leased property?	Value of leased asset (What is the asset worth today?)	
		X 90%	90%
		= 90% of value of leased asset (at lease inception)	
		"Present Value" of lease - This Present Value computation assumes equal annual payments. If this assumption is not correct, preparer is responsible for estimating present value by other means. This is the amount that will be entered into the property system if the lease is determined to be a capital lease.	
Yes/No	Difference		Answer "Yes"
	If the difference is negative the lease is a capital lease.		

**Part C - Conclusion:**

Will this lease be treated as a capital lease?	
Prepared by:	
Date:	
Comments:	

This document must be kept in each official lease file.



## C. Leasehold Improvements

### Introduction

#### Leasehold improvements

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Leasehold improvements are modifications to existing leased real property which will extend its useful life by 2 years or more, improve the property's capacity, or otherwise upgrade the property to serve needs different from those originally intended. The most common example of a leasehold improvement is the build-out of leased office space to make the space operational.

### POLICY

#### Leasehold improvements

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If the project is below the capitalization threshold then the improvement is expensed in the fiscal year completed. However, Service-funded cost of leasehold improvements to buildings, structures and facilities leased by the Service are capitalized if they meet the capitalization threshold and are recorded in the general ledger. The Regional Budget and Finance Officer (BFO) should be notified if the improvement is to be capitalized.

 A copy of the contract that obligates the funds for leasehold improvements project should be submitted to the BFO for record. The BFO will notify the FC of the lease cost and acquisition date, and identify FFS source documents.

Buildings constructed on leased land are not considered leasehold improvements. However, the useful life of a building on leased land should not exceed the lease term.

The useful lives of leasehold improvements on Federal buildings leased through GSA must not exceed the expected period of occupancy. However, the useful lives of leasehold improvements on Service leased space must not exceed the lease term.